Public Information - Requirement of Deposit Guarantee Schemes

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Abstract

Deposit guarantee schemes are organized in order to protect depositors of credit institutions which have not the means to find out about their financial situation, and also to increase banking system stability by avoiding massive withdrawals from credit institutions which appear on suspicion of financial problems. But the mission of such a scheme can't be satisfied in the absence of proper organization activity of public information on deposit insurance parameters.

Trust is an important parameter that is critical for the functionality and performances of the financial sector and for the deposit guarantee schemes. But we don't have to forget that trust is a fragile element and it has to be permanently strengthened by all the institutions and stakeholders that are acting in the financial market.

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JEL classification: G20, G21.

Introduction

The deposit is seen primarily as a means to protect depositors of credit institutions and, secondly, as a means of ensuring banking system stability by preventing excessive withdrawals from credit institutions when there are problems or suspicions to the public on the problems of one or more credit institutions. [2]

The accomplishment of the guarantee schemes depends both on the deposit insurance guarantee in itself and for ensuring adequate public information on the conditions of guaranteed conditions. That means what and how much is guaranteed and how the depositors can obtain compensations for deposits that become unavailable (the compensation's payment methods and terms).

The dynamic of the business environment creates a lot of pressures that could lead to risky decisions and actions both from the part of enterprises, but also from the part of loan and guarantee institutions. The managers are called to make high-stakes decisions under less than ideal conditions, often based on inadequate information and time to engage in extensive analysis (IFC, 2012).

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1. The need for public information on deposit insurance

The knowledge based society is a favorable field for reconsidering the role of human resources within organizations and to design new ways for developing and use of the employees creative potential and diminishing the associated risks.

There are specialists that talk about 'organizations as networks', considering that they represent useful approaches for having new insights into organizational management that can foster the leaders to take more advantage of the organization's resources (Oberg, Walgenbach, 2008; Nicolescu, 2001).

The public sector has a strong cooperation with the private one, especially in what concerns the regulations and protection of the mechanisms that assure the savings, the use and functionality of different financial institutions. They are supported to act not only in the benefits of their shareholders, but also for the well-being of their customers, the depositors.

We can talk about a partnership in a network like structure, where all the involved institutions bring their experience in their struggle for getting a synergetic effect that will profit to all the actors that are involved. In such context, where the innovation can play a crucial role, there are some topics to which the financial institutions' leaders could pay special attention. We are going to emphasize the relationship between the main authority/regulator and the partners in the network, the way in which the main authority/regulator can influence the design, functioning and management of the network, as well as the inter-organizational relationships among partners that could assure mutual benefits and perspectives for competitive evolution in a more globalized market (Baretta, Busco, 2011).

2. Guaranteeing deposit of itself

In the absence of explicit deposit guarantee schemes, when a credit institution went to bankruptcy, the governments or central banks had to provide compensations for the deposits held at credit institutions declared bankrupted. That was used to limit the harmful effects particularly on the economy, arising from the loss of amounts held by depositors, but also by the panic among depositors leading to massive withdrawals of cash that may extend the crisis to other credit institutions, creating new problems.

This behavior of the state is called in the literature usually **implicit guarantee** because, even if it isn't expressly provided for guaranteeing depositors, the public believes that there is the state's obligation to compensate if a bank goes bankrupt and, for reasons of financial stability, the state is really forced to provide financial support to that credit institution (not with an economic justification when the credit institution is insolvent) or even to compensate depositors.

Deposit guarantee schemes are designed in order to strengthen the banking system stability. Numerous studies have shown that the establishment of deposit guarantee schemes resulted in fewer bank failures, and when they occurred, they had less influence on other credit institutions in the system.

Establishment of a Deposit Guarantee Fund provides certainty that depositors will recover payments made with credit institutions (in a given period) and thus their propensity to fast withdraw the amounts they hold to a credit institution over which there arise doubts decreases. Thus we are reducing the risk of liquidity crisis (when suspicions are unfounded).

One of the most important parameters considered when setting up a deposit guarantee scheme is about how to finance it. There is the possibility to finance guarantee scheme ex-ante - by creating first a guarantee fund where the credit institutions, that can attract deposits, will participate in the mandatory rule. And there is the finance guarantee scheme ex-post - by creating amounts required for repayment of depositors, whose deposits became unavailable, only after the appearance of that event.

Advantages of the first method consists in higher reliability, higher capacity to react to pay depositors, reducing the risks of extending crisis because of the large sums' withdrawal from other credit institutions in a short time, which could lead to liquidity problems for some of them.

Another important advantage is that credit institutions, which create problems, are also participating for a while in the fund from which payments will be made. The establishment of increased contributions depending on the risk of bankruptcy can impose a higher cost for higher risk assumed.

The advantages of the second methods lies in blocking the deposit insurance of smaller amounts, which results in obtaining by credit institutions higher profit rates in the periods in which there is no intervention of the guarantee scheme for the compensation's payment.

Another important parameter is **the guarantee coverage**. This parameter primarily involves **defining the categories of depositors covered by deposit insurance** (the most commonly used method is to define exclusions from the guarantee - usually for state institutions, financial institutions, significant shareholders of the credit institution whose deposits become unavailable, and other categories of depositors that can be adequately informed on the financial situation of credit).

Secondly, it involves determining a **guarantee ceiling -** the amount by which full compensation is guaranteed for the deposits held at credit institutions.

Some schemes defined another parameter, the limits that depositor co-insurance can support a portion of deposits held - deposits over a certain limit are compensated, but with a co-insurers deduction rate (usually expressed as a percentage). After the financial crisis in late 2007, this method was considered risky and most guarantee schemes, which have used it, ended in giving up to it.

Finally, another important parameter for deposit insurance is **the period between the declaration of unavailability of deposits and the start of compensation payments** (defined inappropriately as payment period in some literature works). The shorter this period is, the less the depositor suffers and, accordingly, he is less prone to the rapid withdrawal of deposits when doubts arise about the soundness of some credit institutions.

3. Ensuring adequate public information on the conditions of deposit guarantee

In order to achieve the objective of maintaining the banking system's stability it is necessary for depositors to be informed about the conditions in which deposits are guaranteed. It is necessary to ensure adequate visibility for the deposit guarantee scheme.

Without the necessary visibility, the depositors may not be aware that their deposits are guaranteed - in this case they will behave as they would not be guaranteed, or have the wrong expectations on the guarantee. When a credit institution is declared unavailable, they may suffer some losses which could be avoided, or cause problems in the payment process, or it can be created a distorted image of the guarantee scheme.

During the seminar "Building Confidence by Awareness", organized in Bucharest on March 30 to 31, 2011 by IADI (International Association of Deposit Insurers) and FGDB (Deposit Guarantee Fund in the banking system in Romania), on the theme of raising awareness of the public about deposit guarantee schemes, there were presented and discussed experiences of the participants (representatives of the guarantee funds of 17 countries, mainly European, American and Asian and the communication's specialists from commercial banks as National Bank of Romania, Romanian Association of Banks and the Ministry of Finance) about ways of communication on deposit insurance and objectives in this area.

The main **objectives** of the communication departments of institutions which administer deposit-guarantee schemes are the following:

- Setting a target level information on deposit insurance of depositors (percentage of respondents to surveys held regularly).
- Transmission of accurate and understandable messages on the benefits and limitations of deposit insurance.
- Educating the target audience.
- Consumer confidence in banking system.
- Establishing and strengthening a brand image for the deposit insurer to increase financial stability.
- Obtaining feedback from the public.
- Use of appropriate communication channels for different target audiences, refining the message for each of the categories according to their knowledge and interests.
- Detailed planning information campaigns conducted by the insurer of deposits - by mentioning the permanent (information to depositors and potential depositors on deposit insurance) and specific elements for intervention for the compensation payment (when and what information to communicate written and audiovisual media, what information is displayed and where, etc.).
- Strategic partnerships with other members of the network of financial security for concerted campaigns to inform the public.

- Transformation of the uninformed consumer in informed consumer who understands the phenomenon and is involved in running it.

The main **means of communication** used by communication departments of institutions which administer deposit guarantee schemes are the following:

- Creation and development of the organization's site.
- Cooperation with participating credit institutions to the guarantee scheme in order to inform the depositors - these should be the main channel for information to depositors! The direct transmission of information can take many forms by reference to forms of storage of information about deposit insurance, by submitting posters or leaflets about deposit insurance.
- Carrying out research on saving behavior and public awareness of the guarantee scheme.
- Publishing regular bulletins on the subject of deposit insurance and savings, distributed both electronically - through the organization's website and printed - by credit institutions, research institutes, institutes of higher education.
- Publishing articles in professional journals.
- Giving presentations at conferences.
- Media interviews (print, TV, radio).
- Direct answers to public questions (by phone, e-mail, fax, website - a section of frequently asked questions).
- Funding games (distributed free online or call) which simulates the behavior of banking services consumers (eg Malaysia).
- Exhibition on promotional materials that may be offered by insurers of deposits (ex: those held annually by IADI).
- Measure the anxiety of consumers of banking products (which can be a quiet time, anxiety, stress or panic).

The categories of the **target audience for which you have to carry out the information campaigns**[3] are the following:

- Depositors and potential depositors.
- Employees of the institutions that are members of the guarantee scheme.
- Government and regulators.
- Media.
- Professional associations
- Different levels of educational institutions (secondary, secondary, tertiary).

[3] Jean Pierre Sabourin - *Building Confidence by Awareness: Types of Communication and Best Practices,* Prezentare la seminarul "Building Confidence by Awareness", IBR, București, 31 martie 2011

Conclusions

Lack of public information on deposit insurance guarantee scheme renders the organization, because depositors who are not aware of guarantee behave as if their deposits are not guaranteed, emphasizing banking system's instability.

Too aggressive information campaigns can also create some doubt on the soundness of the banking system. We compare the situation to that of a shipping company that advertises insisting that its ships are equipped with enough lifeboats

The tone releases must be submitted according to the news, in order not to alarm consumers, but to inform them and verify that they are covered.

Finding the best information resources (tools used, communication channels) and optimal sizing information campaigns are important tasks of the departments of communication within the institutions in charge of guaranteeing bank deposits.

Specific communication activities have to be planned, by setting frequent communication through various channels, plans to be reviewed and modified based on public reaction monitor results at each stage of ongoing public information campaigns

It is recommended the involvement of outside organization's specialists in order to design and organize events or information campaigns.

It is noted that the public interest for information about deposit insurance increases during the intervention and the insurer of deposits and decreases in time from last intervention (in the absence of reminder campaigns). Information campaigns should be intensified when we see the changing legislation about guaranteeing deposits (especially when they are changing the limits of deposits and the guarantee coverage) or during the depositors payout start of credit institutions.

A well informed public is less susceptible to rumors and public confidence in the safety of deposits is a powerful tool to prevent massive withdrawals from banks. [4]

Informing the public about the benefits and limitations of deposit guarantees is not an option, but a critical component of an effective deposit guarantee scheme.

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